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Supreme Court, U.S.
FILED
AUG 26 1996
CLERK

No. 95-2094

IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

DEAN WITTER REYNOLDS INC.,
a corporation,

Petitioner,

v.

HUDSON T. HARRISON and HARRISON CONSTRUCTION INCORPORATED, a corporation,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

REPLY TO BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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The following is furnished in compliance with Supreme Court Rule 29.6:

Dean Witter Reynolds Inc.

Parent Company: Dean Witter, Discover & Co.

Subsidiaries (except wholly owned)—SPS Transaction Services, Inc.

I.

Respondents' Brief Does Not Explain How A Broker-Dealer's "Control" Extends to an Employee's Concealed Transactions with a Non-Customer That are Beyond the Scope of the Employee's Actual or Apparent Authority.

The important question presented by this case is whether Section 20(a) of the Securities Exchange Act makes broker-dealers *prima facie* liable for fraudulent acts of employees that were so remote from any authorized acts that it was determined as a matter of law that no reasonable person could have believed the employees were acting within the scope of their actual or apparent authority. (App. 79-80.)

Respondents' brief does not deny, and realistically cannot deny, that the holding of the court below is equivalent to making a broker-dealer *prima facie* liable for any fraudulent act of an employee, period. The brief, like the opinion of the Seventh Circuit, is conspicuously lacking in explanation of how Dean Witter had "power to control" the transactions between its employees and Harrison. The brief recites at length facts relating to Dean Witter's control over Carpenter's personal trading account, but fails to explain how such control translates into any control over dealings that the employees *and Harrison* deliberately arranged so as to escape Dean Witter's surveillance.

Respondents' argument rests, as did the court of appeals' opinion, simply on the contention that with more investigation Dean Witter might have uncovered the fraud. Section 20(a) discloses no purpose to impose liability on any such basis; it purports to deal with "con-

trol." Respondeat superior liability also rests fundamentally on the theory that the employer has control over the employee, but recognizes that there are limits to such control. In this case it has been specifically held, as a matter of law, that the fraud practiced on Harrison was beyond those limits. (App. 79-80.) The court of appeals' opinion says, in effect, that such limits are irrelevant to "control" under Section 20(a) and implies that there are no such limits.

Respondent's brief asserts that the statute "charges [a broker-dealer] with the duty to protect public investors by the exercise of caution and to look for signs of machinations." (Br. Opp. 12.) Similarly, the court of appeals spoke of the need "to encourage a continuous high standard of caution by broker-dealers to protect themselves and their clients from the machinations of their own unscrupulous employees." (App. 16.)

The language of Section 20(a) imposes no such duty as that referred to by respondents and the opinion below. The attempt to justify the result in this case by reading Section 20(a) in such a fashion plainly "extend[s] liability beyond the scope of conduct prohibited by the statutory text" and is contrary to the "settled methodology" in § 10(b) cases as expounded in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. ___, 114 S.Ct. 1439, 1448 (1994).

II.

Respondents' Brief Does Not Explain How Reliance That Is Unreasonable for Respondeat Superior Liability Can Support Section 10(b) Liability.

Neither respondents nor the court below has offered any explanation of how respondents' claimed belief in the employees' representations could be unreasonable as a matter of law for purposes of respondeat superior liability but reasonable for purposes of control-person liability predicated on an alleged § 10(b) violation.

Respondents' brief in opposition seems to deny that Dean Witter was found liable because of Harrison's purported reliance on Kenning and Carpenter's apparent authority. (Br. Opp. 16.) But the brief itself confirms that that is exactly what happened. The brief states:

> The investments were believed to be in municipal bonds purchased in a program Kenning presented as, and Harrison believed was, sponsored by Dean Witter . . . . Kenning plausibly explained that Dean Witter chose these controlled persons as eligible for the program because of their standing within Dean Witter . . . . (Br. Opp. 17.)

Those are the very same representations that the Seventh Circuit held in its prior opinion could not reasonably be believed by any prudent person:

> Here the undisputed facts show Harrison did not open an account with Dean Witter but, instead, transferred money to Kenning and Carpenter for them to place in Carpenter's employee account at Dean Witter for subsequent investment. In so doing, Harrison expected to enhance his return by paying the lower commission charged Dean Witter employees, although he was not an employee entitled to that

> benefit. It is clear neither Kenning nor Carpenter had the authority, either actual or apparent, to use the account thusly; Dean Witter's rules expressly forbad it, as would ordinary prudence.
>
> We cannot nor can any reasonably prudent person naturally suppose that Kenning and Carpenter possessed the authority to use the employee account for Harrison's benefit. It simply is not believable that their authority would extend so far. Furthermore, Harrison's transactions with Kenning and Carpenter were not regular on their face and could not appear to be within the ordinary course of business, within the ordinary course of their business, at Dean Witter.

(Pet. 6; App. 79-80.)

Whether respondents needed to resort to such a theory of reliance to prove the Section 10(b) violation is beside the point; that is the theory of reliance they chose and that the jury was permitted to accept. The result is that Dean Witter has been found liable as a "control person" where, as a matter of law, the proof did not show justifiable reliance. There could hardly be a clearer example of: "Allowing plaintiffs to circumvent the reliance requirement" in disregard of "the careful limits on 10b-5 recovery mandated by our earlier cases." *Central Bank*, 114 S.Ct. at 1450.

CONCLUSION

For the reasons set forth in the Petition, Petitioner Dean Witter Reynolds Inc. respectfully urges this Court to grant its Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit.

Respectfully submitted,

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